# Financial Markets

Irving Trust

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A badly oversold bond market searched for an excuse to rally this week and found one. Rumors began to circulate of a major new anti-inflation initiative by the administration. The package was expected to contain proposals for major cuts in spending in the 1981 budget and perhaps some limited form of credit controls. Long-term government prices began to stabilize by midweek and then jumped sharply, by more than 3%, on Thursday.

There were also rumors of a wage and price freeze or mandatory controls, but these seem much less likely for now. It is certainly true that the administration feels significant political momentum developing for taking some action. But it probably believes that this can be relieved at least temporarily by a package of spending cuts, along with additional Federal Reserve action. The administration would like to use any wage and price freeze or mandatory controls only as a last resort. There are two reasons.

First, many economic policymakers in the administration undoubtedly feel that controls won't work. In the short run, the effects of controls always seem to be favorable: The inflation rate does seem to slow, and there may even be some stimulus to economic activity as people buy in advance to beat future price increases after the controls are lifted. But these positive effects don't last very long. Soon, shortages begin to appear, and the consumer discovers that these shortages are even worse than the inflation. It doesn't make much difference that the price of beef isn't going up if there isn't any beef on the supermarket shelf. People also soon find that although prices aren't going up as fast, neither are their own wages. Contention begins to develop as exceptions to the program are allowed, and some products and wages are exempted from the controls or treated more leniently. The second reason to avoid controls is that from a political point of view this is a poor time to apply them. The trick in applying controls is to put them on close enough to an election so that the favorable effects are perceived but before all the problems begin to multiply. At the present time, November is too far away.

The growth of credit extended by the banking system has slowed significantly since the Federal Reserve's actions on October 6. Loans have been rising at only an 8% annual rate versus a 22% rate of increase over the comparable period prior to the change. Over the full year up till October 6, loans were up 20%. These figures are based on all loans (exclusive of money market loans) made by the large weekly reporting commercial banks. Business loans at these same banks have been rising at an annual rate of only 9% since October 6. Credit growth in the banking system does not seem to have been excessive recently. Thus, there is no evidence that additional controls are needed on bank credit expansion. In fact, the Fed already has at its disposal tools to control bank credit, which aren't being used. For instance, the Fed could increase the proportion of bank reserves suppplied at the discount window and exercise window surveillance over the asset growth of banks using this facility.

On the other hand, there has been no slowdown in the rate of commercial paper issuance since October 6. Paper issued by all institutions has been rising at a 34% annual rate since then, just about the same rate of increase as occurred over the prior year. Paper issued by nonfinancial corporations has been increasing at a 49% annual rate.

Gordon B. Pye

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# Money Market Rates

| | 2/29/80 (noon) | Week Ago | Year Ago |
|---|---|---|---|
| Prime Lending Rate at Irving Trust Company | | | |
| Short-term loans to substantial depositors with highest credit rating | 16.75 | 16.25% | 11.75% |
| Effective since | 2/29/80 | | |
| Discount Rate at Federal Reserve Bank | 13.00 | 13.00 | 9.50 |
| Federal Funds | 15.50 | 14.50-15.50 | 10.00 |
| Repurchase Agreements | 13.25 | 13.75 | 9.65 |
| U.S. Treasury Issues - Yields | | | |
| Bills | | | |
| 3 months | 14.55 | 14.18 | 9.75 |
| 6 months | 15.10 | 14.65 | 10.07 |
| 1 year | 15.40 | 15.18 | 10.32 |
| Coupons | | | |
| 2 years | 14.66 | 14.62 | 9.85 |
| 4 years | 13.71 | 14.10 | 9.30 |
| 7 years | 13.08 | 13.30 | 9.22 |
| 10 years | 12.80 | 13.25 | 9.16 |
| Long Bond | 12.29 | 12.85 | 9.08 |
| Negotiable Certificates of Deposit-Secondary Market | | | |
| 1 month | 15.00 | 15.05 | 10.00 |
| 3 months | 15.65 | 15.10 | 10.20 |
| 6 months | 16.05 | 15.35 | 10.60 |
| 1 year | 16.00 | 15.75 | 10.80 |
| Bankers' Acceptances | | | |
| 1 month | 14.95 | 14.90 | 9.90 |
| 3 months | 15.60 | 15.50 | 9.95 |
| 6 months | 16.10 | 16.05 | 10.20 |
| Eurodollar Deposits | | | |
| 1 month | 16.25 | 16.25 | 10.25 |
| 2 months | 16.63 | 16.38 | 10.50 |
| 3 months | 17.00 | 16.63 | 10.56 |
| Commercial Paper - Prime Names | | | |
| Directly placed by: | | | |
| Finance Companies | | | |
| 1 week | 14.00 | 13.25 | 9.00 |
| 1 month | 14.50 | 14.00 | 9.75 |
| 3 months | 14.00 | 13.00 | 9.75 |
| Bank Holding Companies | | | |
| 1 month | 14.63 | 14.25 | 9.75 |
| Dealer Placed: | | | |
| 3 months | 14.88 | 14.30 | 10.00 |
| New Aa Corporate Utility Bond | 14.50 | 14.40 | 9.85 |
| Tax Exempt | | | |
| 6 month Project Notes | 7.00 | 7.10 | 5.15 |
| 12 month Project Notes | N/A | N/A | 5.40 |
| 20 year AAA Bond | 8.50 | 7.95 | 5.85 |

This information represents prevailing market yields. It should not be construed as an offering. All yields are on the offered side of the market.

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